ITEM NO. 1

**PUBLIC UTILITY COMMISSION OF OREGON**
**STAFF REPORT**
**PUBLIC MEETING DATE: March 2, 2006**

**REGULAR** X **CONSENT** ____ **EFFECTIVE DATE** N/A

**DATE:** March 2, 2006

**TO:** Public Utility Commission

**FROM:** Ed Busch EB

**THROUGH:** Lee Sparling ls

**SUBJECT:** Staff Review of PGE Issues Raised by the City of Portland

## STAFF RECOMMENDATION:

Staff recommends the Commission take no action at this time on the issues raised by the City of Portland about PGE, with one exception: that PGE and other regulated electric and natural gas utilities be directed to file the rates they charge customers for local income taxes for Commission review and approval.

## DISCUSSION:

At the direction of the Commissioners, Staff has reviewed the issues raised in a December 6, 2005, memorandum by Portland's City Attorney entitled, "Report on Documents received from Portland General Electric pursuant to Resolution No. 36337 (Substitute)," as well as follow-up issues identified by the Portland City Council. The purpose of our review was to thoroughly evaluate the issues and to determine what action, if any, to recommend the Commission take in response.

Accompanying this memo is a report that presents our analysis and conclusions on six issues.[1] Here, we briefly summarize our findings on each issue.

1. Did PGE keep $88 million collected from customers to pay income taxes?

No. Three adjustments in the analysis should be made. The first makes the treatment of deferred taxes consistent across the study period. The second includes all of 1997 in the analysis as a way to recognize that tax payments are made infrequently. The third

[1] Other Staff contributed to the report. They are: Judy Johnson, Maury Galbraith, Michael Dougherty, and Bryan Conway.

removes the tax liability associated with PGE's non-regulated operations, in order to make a fair comparison between taxes collected in utility rates and taxes paid to Enron. The result is that PGE made payments to its corporate parents or directly to taxing authorities that were about $56 million more than it collected from customers, not $88 million less.

2. Did PGE change the allocation of income from certain wholesale transactions for the 2000 tax year in order to boost its Multnomah County Business Income Tax liability, knowing that any taxes collected would be sent to and kept by Enron?

PGE changed to its treatment of certain transactions called "bookouts" (offsetting purchases and sales where no power actually flowed), assigning those revenues to Multnomah County and increasing tax collections for 2000 by less than $1 million. The company changed its treatment of bookouts for subsequent years, assigning them to delivery points (hubs), all outside the county. We have not seen any evidence that PGE made the change for 2000 to boost tax payments to Enron, and PGE's explanation of the events that transpired is plausible. However, PGE has not provided any contemporaneous documents showing why it made particular decisions about the treatment of bookouts.

The Department of Justice advises that the Commission has authority over the rates regulated utilities charge for local income taxes. We recommend the Commission direct the electric and natural gas utilities to file tariffs for their local income taxes. That will provide a process for formal review and approval of the charges, with input from the public.

3. Can the Commission require refunds of income taxes collected but not paid to taxing authorities?

On the advice of the Department of Justice, the Commission has consistently followed the "filed rate doctrine." That principle states that a regulator cannot order refunds of (or surcharges on) amounts collected under legally approved tariffs. No court has ever found that the rates the PUC set from 1997 through 2005 were illegal because income taxes were calculated using PGE's stand-alone tax liability consistent with long-standing policy. In a letter opinion, a Circuit Court has stated that the amount a consolidated company paid in taxes is not relevant. Beginning with the 2006 tax year, Senate Bill 408 requires that the amount of taxes PGE collects be trued up to the amount of tax payments properly attributed to the company.

4. Did PGE fail to collect $246 million owed to customers by Enron?

No. PGE's claims against Enron were 1) offset by amounts PGE owed back to Enron, 2) eliminated when certain contingencies (potential lawsuits) did not occur, or 3) related to monies belonging to shareholders, not customers. PGE's settlement of the claims with Enron did not harm customers and none of PGE's regulatory accounts or rates was affected.

5. Did customers benefit from the sale of the Coyote Springs 2 site?

Yes. PGE did not need the site to build a generating plant for its customers, and customers have received $10.5 million from the gain on the sale and annual savings of $1.4 million from the shared use of facilities.

6. Did PGE engage in improper trading activity during the energy crisis of 2000-01? Are PGE's rates high today because of trading activity and market conditions during the energy crisis?

In its 2002-2003 investigation, Staff concluded that PGE's involvement in Enron's "Death Star" transactions was minimal and any impact on prices was likely very small. PGE's current rates are not inflated because of power purchased during the energy crisis. PGE's rates remain higher than before 2001 due to the high cost of power supply resources. The main driver is the dramatic increase in natural gas prices, which affect the cost of more than 40 percent of PGE's power supplies. We estimate that PGE's rates would be 1.7 cents per kWh lower if the price of natural gas were at its pre-crisis level.

**PROPOSED COMMISSION MOTION:**

That regulated electric and natural gas utilities file the rates they charge customers for local income taxes for Commission review and approval. Staff does not recommend any other Commission action on the issues discussed at this time.